

Reality Check: Lending Rip-Offs

What is Predatory Lending?

Most lenders are reputable and community-minded and charge a fair price for the use of borrowed money. Unfortunately, there are also a rather small group of lenders, called predatory lenders, who take advantage of others.

- ◆ **Predatory lenders** market to vulnerable populations, such as the elderly, minorities, and people with poor credit histories, and they charge extremely high interest rates and fees.
- ◆ Predatory lending has recently become an increasing problem nationwide. Predatory lenders include both mortgage lenders that prey on homeowners and non-mortgage lenders that offer both secured and unsecured loans.
- ◆ Predatory lenders make money, regardless of whether loans are repaid. Either they:
 - receive loan payments from borrowers, charging high interest rates and up-front fees, or collect high fees from the borrowers and sell the loan, often collecting another fee from the loan purchaser, or
 - **foreclose** on a borrower's home or seize any other property pledged as security (e.g., repossessing a car with a car title loan).
- ◆ **Foreclosure** is a legal process by which a home is taken by a lender for non-payment of a mortgage.

How to Identify Predatory Lenders

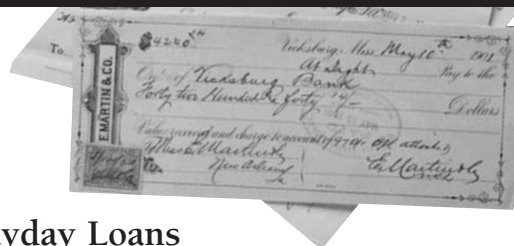
Predatory lenders can take advantage of you, which can often result in the loss of your home and life savings.

- ◆ You are often lent more than you can afford to pay back.
- ◆ Interest rates and fees are well above what is needed to pay the lender for the risk and earn a good profit.
- ◆ Six characteristics of predatory loans, applicable to mortgage loans, include:
 - **High interest rates** (e.g., 20% + interest plus the financing of loan insurance)
 - **Outrageous fees** (one lender charged 25 points; i.e., 25% of loan amount)
 - **High pressure salespeople** (e.g., claims that a loan rate won't last long)
 - **Unaffordable repayment terms** (lenders know that borrowers can't repay)
 - **Harassing collection tactics** (e.g., punitive late fees, abusive callers, etc.).
 - **Deceptive advertisements and practices** (e.g., intentionally overstating a borrower's income)

High Cost Borrowing Practices

Here are some of the most expensive ways to borrow money.

Payday loans (also called paycheck loans, cash-advance loans, fast check loans, or deferred deposit loans)	You write a postdated check (a check with a future date on it) and pay a high fee to a lender to get cash immediately. The check is held by the lender until the future date and then it is cashed or deposited.
Pawnshop loans	You get immediate cash by giving items (such as jewelry and watches) to pawn brokers to hold as security for a loan. Pawn brokers keep the item 30 to 45 days. If you do not pay back the loan plus interest, they can sell your items.
Car title loans	High-interest loans in exchange for possession of your car title. If you don't repay the loan, the car can be repossessed (taken).
Check cashing store	You pay a fee to cash a check. Sometimes these fees can be high.
Advanced fee loan scams	A person or company "guarantees" you'll qualify for a loan if you pay an up-front fee (e.g., \$100 or more). Instead, they take your money and you don't get the loan. This is fraud.
Rent-to-own plans	You rent new or used items (e.g., furniture, appliances) by the week or month. After the item has been rented for a specified period, you own the item.



Payday Loans

- ◆ Small, short-term, high-rate loans (usually made for a 14-day loan period).
- ◆ Fees can be very expensive. Fees are usually calculated by charging a certain amount per face value of the loan, such as \$20 on a \$100 check, which means you pay \$120 to get \$100.
- ◆ If you don't have enough money in your checking account at the end of the loan period, the lender will charge another fee.
- ◆ Payday lenders try to avoid state usury laws that limit the amount of interest a lender can charge for a loan. They do this by calling their charges "fees" instead of "interest." They avoid these limits by starting their company in a state without usury laws.

Check-Cashing Stores

Check-cashing stores are similar to payday lenders. They charge fees to cash checks. This can be an expensive alternative for getting cash, especially if you must cash checks on a regular basis, such as payroll checks. Try not to use check cashers, but if you have to, shop around for the lowest fees.

Alternatives to Check-Cashing Stores

There are reasonable alternatives to check-cashing stores:

- ◆ **Credit Unions**- Credit unions are non-profit financial institutions that serve a group of people with something in common, such as the same employer or church affiliation.
- ◆ **Electronic Transfer Accounts (ETAs)**- This is an account that allows you to receive federal government payments electronically through direct deposit for a cost of \$3 per month or less.
- ◆ **Supermarkets**- Some supermarkets will cash your check for free with a check-cashing card if you buy a certain amount of groceries.

Rent-to-Own Agreements

Before you can take a rent-to-own item out of the store, the store will require you to sign a rent-to-own agreement. This is a contract where you need to read the terms (or guidelines). Consider the following items before signing a rent-to-own agreement:

- ◆ This method of ownership is expensive.
- ◆ Agreements usually consist of a rental contract that is renewed on a weekly or monthly basis.
- ◆ Usually, the terms are for 78 weeks or 18 months.
- ◆ At the end of the agreement, the customer may own the item or need to return it to the store.

Alternatives to Rent-to-Own

There are less expensive options than rent-to-own. When looking at different purchase options, you can:

- ◆ Save up and then buy with cash.
- ◆ Buy with a credit card (if available). If you pay less than the full amount due when the bill comes, you will also pay interest. The total amount you pay will depend on the annual percentage rate (APR) of the credit card and how many billing periods it takes to pay off the purchase.

- ◆ Buy through a store lay away plan. Many retail stores will allow you to make regular payments on an item. The store keeps the item in storage while you make these payments. Usually, you pay a certain up-front fee (depending on the store's policy) and make regular payments for a limited amount of time. At the end of the payment period, you can pick up the item at the store. The store may charge an additional handling fee, but this is still less expensive than rent-to-own.
- ◆ Save money for a month to put down on an item, and then put it on layaway or buy on credit.
- ◆ Consider buying a used item from a second-hand store or yard sale.
- ◆ Before you buy anything, ask yourself "Do I really need this item now?" Unfortunately in our culture today, many wants are being marketed as if they are needs and we are encouraged to have now and pay later. You might not need it or you might be able to wait until you save the money to purchase it with cash.

Compare the Costs of Buying Options

There are many ways to buy large items, such as electronics, appliances, or furniture. Use the following list and chart to help you decide which purchase option is best for you before you buy:

- ◆ Make sure you are comparing the same item, make, and model in advertisements and local retail stores. For example, in the case of an HD-TV (high definition television), there are many different makes and models to choose from, and these will have a wide range of prices, depending on the features available.
- ◆ Using the chart below, look at the second row, "Time to pay off." This is how to work out what goes in each column:
 - Rent-to-Own - the number of rental payments until the item is owned.
 - Credit - the number of payments until the credit is paid off.
 - Layaway - the number of payments until the item is paid off. Some stores add a service fee and some do not.
 - Cash - zero, since there are no payments.
- ◆ In the third row, look for the "Initial payment required" by the "Rent-to-own contract" or the "Layaway" plan. Some stores add service fees to the initial payment.
- ◆ For the "Total paid," multiply the "payment" by the "Time to pay off" and then add the "Initial payment required."
 - For "Cash (Local Retail Store)," use the cash price.
- ◆ For "Amount above cash price," subtract the "Cash price" from "Total paid" for each option. This will tell you how much more you are paying above the original cash price of the item.


Item: Tower of Power Mini Stereo System with CD Player	Rent-to-Own	Credit	Layaway	Cash (Local Retail Store)
Cash price	\$521.56	\$330.00	\$330.00	\$330.00
Time to pay off	22 months	20 months	3 months	0 months
Initial payment required	\$11.99	\$20.00	\$35.00 (a \$5.00 service fee is required)	\$330.00
Weekly/monthly Payment	\$47.96/month	\$20.00/month	\$100.00/month	\$0
Total to be paid	\$1,039.00	\$381.99	\$335.00	\$330.00
Amount above original cash price	\$517.44	\$51.99	\$5.00	\$0

(Rent-to-Own APR=100%; Credit APR=18%)

How to Avoid Rip-Offs

- ◆ Find out how much a loan will cost you over time. Compare at least three lenders before making a decision.
- ◆ Always check out a lender before signing loan documents, especially if he/she contacted you first and they are not located in the city or county where you live.
- ◆ Check out lenders by asking friends, relatives, and co-workers. They may have had experience with a particular lender or know someone else who has.
- ◆ Call the Better Business Bureau (BBB). To get the name of the Better Business Bureau closest to you, visit www.bbb.org.
- ◆ Local or state consumer protection agencies can provide information about any complaints about a particular lender.
- ◆ Ask lots of questions and be suspicious of anyone who threatens to withdraw the loan if you don't keep quiet.

Remember, if a loan sounds too good to be true, it probably is. Trustworthy lenders do not go door-to-door or lend more than borrowers can afford to repay.



Predatory Lending Learning Extensions

1. Search the newspaper for the familiar phrase, "Buy now, pay later!" There are usually a number of advertisements for furniture, electronics, automobiles, and mobile homes that use this phrase. Why does it appeal to a large segment of our population? What interest rates and service fees are listed in each ad? How could you make the best out of a buy now, pay later option?
2. Quiz.
 - a) Fees charged for payday loans are a certain _____ of the face value of the loan.
 - b) Another name for payday loans _____
 - c) How long is the usual payday loan period? _____
 - d) If you have a payday loan, you do not want it to _____
 - e) Payday loans may avoid which state law? _____
3. Choose an item such as a DVD player that rent-to-own stores typically have. Search through the newspaper to find advertisements for rent-to-own plans or visit a rent-to-own site on the Web. Fill out the following chart to compare the costs of the available options. For the credit option use 18%, use the same time period as it will take for the rent-to-own, and one of the financial calculators on pages 6 & 7 to figure the payment. (Review the example on this page) You may have to call a store to check on layaway options and fees

Item: Television or DVD player	Rent-to-Own	Credit	Layaway	Cash (Local Retail Store)
Cash price				
Time to pay off				
Initial payment required				
Weekly/monthly Payment				
Total to be paid				
Amount above original cash price				